FINANCIAL REGULATION: 2011 Q2

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Introduction

In 2011 Q2 a relatively small number of new financial provisions was promulgated in comparison with previous periods.

In the field of financial institutions, Spanish solvency law was amended to adapt it partially to recent Union legislation. The opportunity was taken to introduce a new legal regime governing additional contributions to credit institution deposit guarantee funds based on the remuneration of these instruments.

Also, amendments were made to adapt Spanish law on payment and securities settlement systems to Union legislation, particularly to recognise so-called "interoperable systems" and to extend to them the legal provisions on settlement finality in credit transfer orders.

In the European Union area, there were four notable new provisions: the amendment of TARGET legislation to enable the ECB to provide overnight credit to certain counterparty institutions not licensed as credit institutions; the regulation of mergers of public limited companies in order to unify the protection of shareholders' and third parties' interests in these processes in Member States; the updating of legislation on purchases of euro banknotes; and the amendment of the EU regulation on credit rating agencies to include the functions acquired by the new European Securities and Markets Authority.

Within the securities market, there were three new pieces of legislation: the adaptation of Spanish law to EU legislation on credit rating agencies; certain changes to the information required of foreign collective investment institutions registered in the CNMV registers; and the updating of collective investment institution categories based on investment policy.

Finally, a new law on consumer credit agreements writes into Spanish law the recent European legislation in this connection.

Amendment of the law on credit institutions' own funds and on credit institution deposit guarantee funds

Law 6/2011 of 11 April 2011 (BOE of 12 April 2011) amended Law 13/1985 of 25 May 1985[1] on investment ratios, own funds and reporting requirements for financial intermediaries, Law 24/1988 of 28 July 1988[2] on the securities market and Legislative Royal Decree 1298/1986 of 28 June 1986[3] on the adaptation of current credit institution law to EU legislation.

The purpose of the Law is to commence transposition of Directive 2009/111/EC of the European Parliament and of the Council of 16 September 2009 amending Directives 2006/48/EC, 2006/49/EC and 2007/64/EC as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements, and crisis management.

1 See "Regulación financiera: segundo trimestre de 1985", *Boletín Económico,* July-August 1985, Banco de España, pp. 51 and-52.
2 See "Regulación financiera: tercer trimestre de 1988", *Boletín Económico,* October 1988, Banco de España, pp. 61 and-62.
3 See "Regulación financiera: segundo trimestre de 1988", *Boletín Económico,* July-August 1988, Banco de España, pp. 45 and-46.

More recently, *Royal Decree 771/2011 of 3 June 2011* (BOE of 4 June 2011) amended Royal Decree 216/2008 of 15 February 2008[4] on financial institutions' own funds and Royal Decree 2606/1996 of 20 December 1996[5] on credit institution deposit guarantee funds.

This Royal Decree implements Law 2/2011 of 4 March 2011 on sustainable economy and Law 6/2011 of 11 April 2011. It also makes headway in the transposition of Directive 2009/111/EC and of Directive 2010/76/EU of the European Parliament and of the Council of 24 November 2010[6] amending Directives 2006/48/EC and 2006/49/EC as regards capital requirements for the trading book and for resecuritisations and the supervisory review of remuneration policies.

It also takes the opportunity to introduce a new legal regime governing additional contributions to credit institution deposit guarantee funds based on the remuneration of the deposits, in line with the provisions being adopted in this connection in the EU.

The most noteworthy developments from the standpoint of financial regulation are as follows:

SECURITISATION

Law 6/2011 makes it compulsory for credit institutions and investment firms to meet certain requirements to allow them to assume exposures to securitisation positions and to initiate such securitisation.

Under these requirements, which are set out in Royal Decree 771/2011, a credit institution, other than when acting as an originator, a sponsor or original lender, shall be exposed to the credit risk of a securitisation position in its trading book or non-trading book only if the originator, sponsor or original lender has explicitly disclosed to the credit institution that it will retain, on an ongoing basis, a material net economic interest.

For these purposes, "retention of net economic interest" means: a) retention of no less than 5% of the nominal value of each of the tranches sold or transferred to the investors; b) in the case of securitisations of revolving exposures, retention of the originator's interest of no less than 5% of the nominal value of the securitised exposures;[7] c) retention of randomly selected exposures, equivalent to no less than 5% of the nominal amount of the securitised exposures, provided that the number of potentially securitised exposures is no less than 100 at origination; or d) retention of the first loss tranche and, if necessary, other tranches having the same or a more severe risk profile than those transferred or sold to investors and not maturing any earlier than those transferred or sold to investors, so that the retention equals in total no less than 5% of the nominal value of the securitised exposures.

The Banco de España may specify the conditions of application of this Law and how those institutions will communicate the retention requirement to investors. This communication must allow them ready access to all pertinent data on exposures. Also, the Banco de España may opt to suspend temporarily the aforementioned requirements during periods of general market liquidity crisis.

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4 See «Financial Regulation: 2008 Q1», *Economic Bulletin*, April 2008, Banco de España, pp. 159-163.

5 See "Regulación financiera: cuarto trimestre de 1996", *Boletín Económico,* January 1997, Banco de España, pp. 106-109.

6 See «Financial Regulation: 2010 Q4», *Economic Bulletin*, January 2011, Banco de España, pp. 153-155.

7 Securitisations of revolving exposures are those whereby investors remain fully exposed to all future draws by borrowers so that the risk on the underlying facilities does not return to the originator credit institution even after an early amortisation event has occurred.

As an exception to the foregoing, this Law will not apply where the securitised exposures are claims on assets unconditionally and irrevocably guaranteed by: a) central governments or central banks; b) regional governments, local authorities and public sector entities of Member States; c) institutions to which a 50% risk weight or less is assigned under Royal Decree 216/2008; or d) multilateral development banks.

In addition, the Law establishes monitoring and reporting obligations on institutions investing in securitisation instruments. Thus credit institutions shall have a comprehensive and thorough understanding of each of their individual securitisation positions and demonstrate that they have implemented therein formal policies and procedures appropriate to their trading book and non-trading book and commensurate with the risk profile of their investments. To comply with this obligation, the Banco de España shall determine the items which, as a minimum, have to be examined and recorded by institutions, including stress tests and how they are to be carried out.

Originator and sponsor credit institutions shall apply to the exposures they intend to securitise the same credit standards and credit management criteria applied to the exposures they intend to hold in their portfolio, in accordance with the technical criteria on the organisation and treatment of risk stipulated by the Banco de España. Moreover, they shall inform investors of the level of their commitment to maintaining a net economic interest in the securitisation. Further, they shall ensure that prospective investors have readily available access to all relevant data as stipulated by the Banco de España.

Finally, the consequences of failing to comply with the requirements regarding securitisation positions are set out. If a credit institution does not comply with its obligation to communicate its retention requirements, the risk weight of its securitisation exposures shall be increased, the Banco de España determining the extent of such increase and how it is to be applied. If the due diligence conditions established by the Banco de España are not met, the originator credit institution may not exclude the securitised exposures in the calculation of its capital requirements.

CHANGE IN THE REQUIREMENTS FOR PREFERENCE SHARES TO BE ELIGIBLE AS OWN FUNDS

In order to adapt the legal regime governing credit institution preference shares[8] to international requirements and thus ensure they are an effective instrument for meeting solvency requirements, Spanish legislation has been changed in certain respects.

Specifically, the issuance conditions may not include early redemption incentives and must set the remuneration to which the securityholders are entitled, provided always that it shall be conditional on the existence of distributable profit or reserves. The Board of Directors or equivalent body of the issuing or parent credit institution has the power to cancel, at its discretion, when necessary, the payment of interest or dividends for an unlimited period of time, on a non-cumulative basis. Payment may also be cancelled if the issuing or parent credit institution or its consolidatable group or sub-group does not meet the minimum capital requirements. In any event, the Banco de España may require the cancellation of remuneration payments based on the financial and solvency situation of the issuing or parent credit institution or on that of its consolidatable group or sub-group.

Also, a mechanism should be established to ensure that preference shareholders participate in the absorption of present or future losses of the issuer or controlling institution.

8 The legal regime governing preference shares is extended to investment firms and, accordingly, references to the Banco de España and to credit institutions, respectively, are understood to also be to the CNMV and to investment firms.

That mechanism should be defined clearly and not hinder possible recapitalisation processes, whether they be through the conversion of preference shares into ordinary shares, non-voting equity units or capital contributions to credit cooperatives, or through the reduction of the nominal value.

The mechanism must be applied in either of the following circumstances: a) where the issuing or parent institution, or its consolidatable group or sub-group, has an original own funds ratio, calculated in the same way as the solvency ratio, below 4% (the Banco de España may set any other solvency ratio provided it is more demanding), or b) where the issuing or parent institution, or its consolidatable group or sub-group, has an original own funds ratio below 6% and material accounting losses.[9]

When the mechanism is that of conversion into ordinary shares, non-voting equity units or capital contributions to credit cooperatives of the issuing or parent credit institution, the issuer has to allow immediate conversion and specify an exchange ratio which sets a floor on the number and nominal amount of shares to be delivered. When the mechanism consists in reducing the nominal amount of the preference shares, the losses incurred by the issuer shall be apportioned between total capital and reserves, on the one hand, and total preference shares outstanding, on the other.

The Banco de España may specify the preference share conversion conditions in accordance with the aforementioned criteria and the manner of determining the losses and the other indicators stated, particularly in the case of issues guaranteed by various institutions, on the basis that the stipulated loss absorption mechanisms do not hinder possible recapitalisation processes.

The limit on the outstanding nominal amount of preference shares remains at 30% of the original own funds of the consolidatable group or sub-group of the controlling entity of the issuing subsidiary, including the amount of the issue itself, without prejudice to any additional limitations that may be imposed for solvency purposes. However, from now on, the Banco de España may change this percentage, although it may never exceed 35%.

Preference shares continue to be perpetual and the issuer continues to have the option of agreeing to early redemption from the fifth year after they were paid in, following prior authorisation from the Banco de España. From now on, this authorisation is subject to the financial situation or solvency of the credit institution or its consolidatable group or sub-group being unaffected. It may also be made subject to the institution replacing the redeemed preference shares with eligible capital items of the same or higher quality.

In this respect the Banco de España may authorise at any time the early redemption of dated or undated instruments in the event of any change in the fiscal regime or in the eligibility of such instruments as own funds that was not envisaged at the issue date.

The payment of remuneration may be replaced, if so stipulated in the terms of issue, by the delivery of ordinary shares of commercial banks or non-voting equity units of savings banks or capital contributions to credit cooperatives, provided that this enables the institution to preserve its financial resources.

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9 Losses are defined as material when those accumulated over the past four quarters have reduced the intitutions's capital and prior reserves by one-third.

This delivery of capital instruments will only be permissible if it produces the same economic result as redemption, i.e. if it does not entail the reduction of capital of the institution,[10] and the issuer has full discretion to opt not to pay the remuneration in cash and, furthermore, may cancel delivery of the capital instruments when necessary.

Lastly, the transitional regime envisaged in Law 6/2011 is implemented, such that the preference shares issued before the entry into force of this Law (13 April 2011) and not meeting the requirements under it may continue to be eligible as the own funds of credit institutions and of their groups, subject to certain limits detailed in Royal Decree 771/2011.

CHANGE IN LIMITS ON LARGE EXPOSURES

The new legislation generally maintains the limit such that the value of all the exposures of a credit institution to a customer (entity or economic group) may not exceed 25% of its own funds.

Where that customer is a credit institution or investment firm, or where the economic group includes one or more credit institutions or investment firms, the value of all exposures may not exceed 25% of the credit institution's own funds or €150 million, whichever the higher, provided that the sum of exposure values to all customers in the economic group that are not credit institutions or investment firms does not exceed 25% of the credit institution's own funds.

Where the amount of €150 million is higher than 25% of the credit institution's own funds, in accordance with the policies and procedures to manage and control concentration risk, the value of the exposure shall not exceed a reasonable limit in terms of the credit institution's own funds. That limit shall not be higher than 100% of the credit institution's own funds.

The previous limit that total large exposures could not exceed 800% of the credit institution's own funds is eliminated.

The following exceptions to limits on large exposures are also eliminated: 1) holdings in certain insurance companies up to a maximum of 40% of own funds, and 2) claims on certain central governments and central banks of countries that are denominated and financed in the borrower's national currency.

CHANGES IN LIQUIDITY RISK MANAGEMENT POLICY

A substantial change was made to the risk management policy of credit institutions, specifically that regarding liquidity risk. The Banco de España will periodically assess the overall management of this risk and encourage the development of sound internal methodologies. Its assessments shall take into account the role played by credit institutions in financial markets. However, the Banco de España shall detail the method and procedure to be used in these assessments.

Credit institutions shall establish robust strategies, policies, processes and systems for the identification, measurement, management and monitoring of liquidity risk over an appropriate set of time horizons, including intra-day, so as to ensure that credit institutions maintain adequate levels of liquidity buffers. Those strategies, policies, processes and

10 The delivery of capital instruments is only considered to produce the same economic result as redemption if the payment in kind is made with capital instruments issued for that purpose and the issuer's obligation is limited to the issuance of such instruments, but neither the issuer nor any of the firms in its economic group undertakes to find purchasers of the instruments or to assume any risk relating to the sale or to the value of the instruments delivered.

systems shall be tailored to business lines, currencies and entities and shall include adequate allocation mechanisms of liquidity costs, benefits and risks.

Credit institutions shall consider different liquidity risk mitigation tools, including a system of limits and liquidity buffers in order to be able to withstand a range of different stress events and an adequately diversified funding structure and access to funding sources. Those arrangements shall be reviewed regularly.

As under the previous legislation, alternative scenarios shall be considered and the assumptions underlying decisions concerning the funding position shall be reviewed regularly.

Credit institutions shall adjust their strategies, internal policies and limits on liquidity risk and develop effective contingency plans, taking into account the outcome of the alternative scenarios considered.

CREDIT INSTITUTION REMUNERATION POLICIES

In accordance with the transposition of Directive 2010/76/EU of the European Parliament and of the Council of 24 November 2010, credit institutions have to apply certain requirements for those categories of staff whose professional activities have a material impact on their risk profile at group, parent and subsidiary levels.

Most notable among other requirements are the following: a) a list indicating the categories of the aforementioned staff must be submitted to the Banco de España ; b) the remuneration policy is consistent with sound and effective risk management, does not encourage risk-taking that exceeds the level of tolerated risk of the credit institution and incorporates measures to avoid conflicts of interest; c) the management body adopts and periodically reviews the general principles of the remuneration policy at least annually, and the implementation of the remuneration policy is subject to central and independent internal review for compliance with the remuneration policies and procedures in place; d) staff engaged in control functions are independent from the business units they oversee, and are remunerated in accordance with the achievement of the objectives linked to their functions; and e) the remuneration of the senior officers in the risk management and compliance functions is directly overseen by a remuneration committee or, if such a committee has not been established, by the relevant management body.

The new legislation regulates the design of remuneration schemes, in which the fixed and variable components should be appropriately and efficiently balanced. The variable remuneration components should be sufficiently flexible such that their adjustment includes the possibility to pay no variable remuneration component.

For these purposes, the Banco de España may establish specific criteria for determining the appropriate proportion between fixed and variable components. The variable remuneration components should create incentives aligned with the long-term interests of the institution and meet certain requirements set out in Royal Decree 771/2011.

The remuneration schemes of credit institutions which receive government financial support for restructuring purposes have to meet, in addition to the foregoing requirements, the following ones: a) where variable remuneration is incompatible with a sound capital base and with an appropriate waiver of government support, it shall be strictly limited to a percentage of net income and b) the directors and managers who effectively direct the activity of the institution may not receive variable remuneration unless it is duly justified in the opinion of the Banco de España, which may, moreover, set limits on their total remuneration.

Most of the remuneration policy is extended to investment firms, such that the references to the Banco de España and to credit institutions shall be deemed to be to the CNMV and to investment firms, respectively.

STRENGTHENING OF THE COMPETENCE OF AND COOPERATION BETWEEN SUPERVISORS

The Law introduces various measures in this respect, such as the obligation of the Banco de España and the CNMV to take into account the effect of their decisions on the stability of the financial stability of other Member States, the regulation of colleges of supervisors and of common decisions within the framework of supervision of cross-border groups, and the possibility of designating a branch of a credit institution as being significant.

Along these lines, to the competences entrusted to the Banco de España and the CNMV as the authorities responsible supervising credit institutions and investment firms, respectively, and their respective consolidatable groups, are added the following new ones:

1 Require institutions and their groups to have in place remuneration policies and practices that are consistent with and promote sound and effective risk management and to limit variable remuneration when it is inconsistent with the maintenance of a sound capital base.

2 Use the information received in accordance with the disclosure criteria established in this Law to compare remuneration trends and practices.

3 Collect information on the number of individuals per credit institution in pay brackets of at least €1 million including the business area involved and the main elements of salary, bonus, long-term award and pension contribution.

That information shall be forwarded to the European Banking Authority and the European Securities and Markets Authority by the Banco de España and the CNMV, respectively.

Regarding European Union supervisory authorities, the new obligations set for the Banco de España and the CNMV include the following:

1 Planning and coordination of supervisory activities in cooperation with the competent authorities involved, in preparation for and during emergency situations, including adverse developments in credit institutions or in financial markets, using, where possible, existing defined channels of communication for facilitating crisis management.[11]

2 The formulation of applications to the competent supervisory authorities of a credit institution or investment firm authorised in the European Union with branches in Spain for such branches to be deemed to be significant, and, in the absence of a joint decision in this respect, the issuance of a decision on whether the branch is significant.

Regarding this latter case, in accordance with the legally stipulated procedure, the Banco de España or, as applicable, the CNMV shall work towards the adoption of a joint decision on the application with the other competent authorities of other Member States entrusted with supervising the various institutions forming part of the group. Also, they shall be re-

11 The planning and coordination of supervisory activities shall include the preparation of joint assessments, the implementation of contingency plans and communication to the public.

sponsible for ruling, through a joint decision, on the equivalent applications made by the competent authorities of countries in which branches of Spanish credit institutions are located, and, in the absence of a joint decision in that respect, for recognising the decision by such competent authority on the branch's significant nature. In these procedures, a branch shall be considered to be significant on the basis of such reasons as market share in terms of deposits, the likely impact of a suspension or closure of the operations on market liquidity or on the payment and clearing and settlement systems, and the size and the importance of the branch in terms of number of clients.

Also, the Law strengthens the close cooperation with other competent authorities responsible for the supervision of foreign credit institutions or investment firms, parents, subsidiaries or investees in the same group. Within this cooperation framework, the Banco de España and, where applicable, the CNMV shall do everything in their power to reach a joint decision to determine the adequacy of the consolidated level of own funds held by the group with respect to its financial situation and risk profile and the required level of own funds for each entity within the banking group and on a consolidated basis. The joint decision shall also duly consider the risk assessment of subsidiaries performed by relevant competent authorities. The joint decision shall be adopted according to the legally stipulated procedure.

In order to facilitate the exercise of their tasks with other EU competent authorities, the Banco de España and the CNMV shall establish colleges of supervisors and ensure appropriate coordination and cooperation with third-country competent authorities.

Colleges of supervisors shall provide a framework for the following tasks, among others: 1) exchanging information; 2) agreeing on voluntary entrustment of tasks and voluntary delegation of responsibilities where appropriate; 3) determining supervisory examination programmes based on a risk assessment of the group; 4) increasing the efficiency of supervision by removing unnecessary duplication of supervisory requirements; and 5) consistently applying the prudential requirements for the taking up and pursuit of the business of credit institutions across all entities within a banking group without prejudice to the options and discretions available in EU legislation;

When the Banco de España or the CNMV supervise an institution with significant branches, they shall also establish and preside a college of supervisors to facilitate the exchange of information. Legal provisions may be promulgated specifying the characteristics to be met by these colleges, the composition of which shall be determined by the Banco de España or the CNMV, as appropriate.

Lastly, the Law reforms the exchange of information by the Banco de España with central banks and other bodies with a similar function in their capacity as monetary authorities. Under this reform, which addresses the exchange of information and cooperation between supervisory authorities, it is expressly provided that such exchange may refer to the information relevant for the exercise of their respective statutory tasks.

AMENDMENT OF LEGISLATION ON CREDIT INSTITUTION DEPOSIT GUARANTEE FUNDS

Royal Decree 771/2011 amends Royal Decree 2606/1996 by introducing a new regime for additional contributions to these funds based on the remuneration of the deposits in them.[12] Specifically, the amounts of the deposits whose agreed remuneration exceeds the

12 Currently the annual contributions of the institutions belonging to the funds are 2‰ of the deposits at year-end covered by the guarantee. The base used for the calculation is the guaranteed deposits plus 5% of the market value on the last trading day of the year, in the relevant secondary market, of the guaranteed securities existing at year-end.

limits specified below shall be weighted at 500% (i.e. 400% more than the weight they would have if they were included in that base) for the purpose of calculating the contributions of the credit institutions belonging to the related deposit guarantee funds.

The limits above which the new weights will be applied are as follows: 1) sight deposits whose annual interest paid in the periodic settlement of the account is more than 100 basis points higher than average 1-month EURIBOR; 2) time deposits (or similar instruments) up to three months whose agreed annual interest is more than 150 basis points higher than average 3-month EURIBOR; 3) time deposits (or similar instruments) between three months and one year whose agreed annual interest is more than 150 basis points higher than average 6-month EURIBOR; and 4) time deposits (or similar instruments) with a term of one year or more whose agreed remuneration is more than 100 basis points higher than average 12-month EURIBOR.

Banco de España Circular *CBE 3/2011 of 30 June 2011* (BOE of 2 July 2011) on additional contributions to deposit guarantee funds sets out technical provisions implementing the new precepts introduced by Royal Decree 771/2011.

The Circular contains two types of rules: those for identifying what is understood as deposit remuneration in different practical cases, and those regulating ad hoc tools for calculating the additional contribution.

Deposit remuneration shall comprise any explicit or implicit compensation or payment, in cash or in kind, for maintaining a deposit. Thus the value of remuneration in kind shall be that applicable under tax legislation, including any tax prepayments to be made for the remuneration when they are borne by the institution. In variable-rate time deposits, the remuneration shall be that which results from applying the reference index at the deposit placement date over the whole of the agreed time period, disregarding possible future modifications. In time deposits in which the interest rates change before maturity, the interest rate taken shall be the average of the rates, weighting each by the time it is to be applied. In hybrid financial instruments in which the embedded derivative does not share similar characteristics and risks with the host contract, the interest rate used to determine their remuneration shall be the maximum annual percent remuneration receivable by the depositor on the amount deposited, if it is higher than the effective annual interest rate corresponding to the host contract after the embedded derivative has been stripped out; in the absence of the former, only the latter shall be taken. In any event, any additional remuneration envisaged in the contract, be it in cash or in kind, has to be included.

For the purpose of calculating the additional contributions to a deposit guarantee fund stipulated in Royal Decree 771/2011, in sight deposits the specified limits shall be compared with the remuneration of their average balances. These average balances shall be the result of dividing the sum of the daily balances of each sight deposit by the number of calendar days included in each settlement. In time deposits, comparison shall be with the various limits set depending on the duration of the initially agreed deposit, disregarding any potential partial repayments agreed in the contract. Subsequent renewals, whether envisaged or not in the original contract, shall be considered as new deposits.

Law 6/2011 came into force on 13 April 2011, Royal Decree 771/2011 came into force on 5 June 2011 (except as provided in the case of the transitional regimes envisaged therein) and Circular 3/2011 came into force on 4 July 2011.

Amendment of legislation on payment and securities settlement systems

Law 7/2011 of 11 April 2011 (BOE of 12 April 2011) amended Law 41/1999 of 12 November 1999[13] on payment and securities settlement systems and Royal Decree-Law 5/2005 of 11 March 2005[14] on urgent reforms to boost productivity and improve public procurement.[15]

The purpose of this Law is to transpose Directive 2009/44/EC of the European Parliament and of the Council of 6 May 2009[16] amending Directive 98/26/EC on settlement finality in payment and securities settlement systems and Directive 2002/47/EC on financial collateral arrangements as regards linked systems and credit claims. More specifically, this Law is intended to recognise so-called interoperable systems and extend to them the legislation on settlement finality of credit transfer orders given through these systems.

The main changes are as follows:

The definition of "credit transfer order" is updated to read as follows: 1) any instruction by a participant[17] to place at the disposal of a recipient an amount of money by means of a book entry on the accounts of a credit institution, a central bank, a central counterparty or a settlement agent; 2) any instruction which results in the assumption or discharge of a payment obligation as defined by the rules of the system; or 3) any instruction by a participant to transfer ownership of or any other claim on one or more securities by means of an entry in a register or other way of accrediting transfer.

Law 41/1999 is amended to provide for so-called "interoperable systems", which are two or more systems whose system operators have entered into an arrangement with one another that involves cross-system execution of transfer orders. System operators may in turn act as settlement agent, central counterparty or clearing house. An arrangement entered into between interoperable systems shall not constitute a system.

The new Law extends to interoperable systems the rules on the irrevocability and finality of settlement of transfer orders given through such systems. In this respect, each system shall determine in its own rules the time when transfer orders become irrevocable and final and shall, to the extent possible, ensure that systems are coordinated in order to avoid legal uncertainty in the event of default of a participating system. However, unless expressly provided for by the rules of all the systems that are party to the interoperable systems, one system's rules on the moment of irrevocability and finality shall not be affected by those of the others.

The new Law also extends to interoperable systems the legal regime under Law 41/1999 for insolvency of a system participant, the procedures established and the effects on transfer orders and on collateral. It should be noted that the opening of an insolvency proceeding against a participant or operator of an interoperable system does not prevent the funds or securities

13 See «Financial Regulation: 1999 Q4», *Economic Bulletin*, January 2000, Banco de España, pp. 103-104.

14 See «Financial Regulation: 2005 Q1», *Economic Bulletin*, April 2005, Banco de España, pp. 115-118.

15 This Law transposes Directive 2009/44/EC of the European Parliament and of the Council of 6 May 2009 amending Directive 98/26/EC on settlement finality in payment and securities settlement systems and Directive 2002/47/EC on financial collateral arrangements as regards linked systems and credit claims.

16 See «Financial Regulation: 2009 Q2», *Economic Bulletin*, July 2009, Banco de España, pp. 183-184.

17 For these purposes, participants shall be understood to be credit institutions and investment firms, the Treasury and its equivalent regional government bodies, and the entities belonging to the public sector, as well as any enterprises whose management is mainly located outside the European Union and whose functions are those of European Union credit institutions or investment companies, which are accepted as system members under the applicable regulations and which are liable to the system for financial obligations derived from its functioning.

available in that participant's liquidation account from being used to meet its obligations in that system during the business day in which the insolvency proceeding was opened.

As regards Royal Decree-Law 5/2005, credit claims[18] are included as part of the collateral that can be used in financial transactions. However, credit claims in which the debtor is a consumer, a micro enterprise or a small enterprise may not be used as financial collateral, save where the collateral taker or the collateral provider of such credit claims is one of the institutions listed in Royal Decree-Law 5/2005.[19]

It continues to be legally required that financial collateral agreements be in writing, or in a legally equivalent form, with no further requirement for their creation, validity, perfection, priority, enforceability or admissibility as evidence. The creation of the security interest shall require, in addition to registration of the collateral agreement, the provision of the asset designated as collateral, and registration of such provision in writing or in a legally equivalent form. However, in the case of credit claims, the inclusion in a list of claims submitted in writing, or in a legally equivalent manner, to the collateral taker is sufficient to identify the credit claim and to evidence the provision of the claim provided as financial collateral between the parties and against the debtor or third parties. A debtor that pays before being notified of the provision of a security interest shall be released from the related obligation.

Debtors of credit claims may validly waive, in writing or in a legally equivalent manner: 1) their rights of set-off vis-à-vis the creditors of the credit claim and vis-à-vis persons to whom the creditor assigned, pledged or otherwise mobilised the credit claim as collateral; and 2) their rights arising from banking secrecy rules.

Regarding the rights of substitution and disposal of collateral provided for in Royal Decree-Law 5/2005, the right of disposal shall not apply when the collateral is a credit claim and the right of substitution shall not apply when the collateral is a non-fungible credit claim.[20]

In the event of enforcement of collateral arrangements by the collateral taker due to non-compliance with the obligations or any enforcement event agreed by the parties, when the collateral is in the form of credit claims, these shall be realised by sale or appropriation and by setting off their value against, or applying their value in discharge of, the relevant financial obligations.

Finally, the rest of the text of Royal Decree-Law 5/2005 is revised so as to correct and clarify other matters not relating to the transposition of the directive, and to resolve some problems of legal uncertainty.

In addition, Law 22/2007 of 11 July 2007 on the distance marketing of consumer financial services was amended. Specifically, the consumer's prior consent is required for a supplier to use automated calling systems without human intervention or fax messages as a means of distance communication.

The Law came into force on 1 July 2011, except for the amendment to Law 22/2007, which came into force on 13 April 2011.

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18 Credit claims are defined as pecuniary claims arising out of an agreement whereby a credit institution grants credit in the form of a loan.

19 Specifically, the ECB, the Banco de España, the central banks of the Member States of the EU, the central banks of third-party States, the Bank for International Settlements, the multilateral development banks, the International Monetary Fund and the European Investment Bank.

20 A credit claim is non-fungible if it cannot be replaced by another of like nature.

Update of TARGET2 legislation

Guideline ECB/2011/2 of 17 March 2011 (OJ L of 1 April 2011) amended Guideline ECB/2007/2 of 26 April 2007[21] on a Trans-European Automated Real-time Gross settlement Express Transfer system (TARGET2) so that the ECB Governing Council may, as a precautionary measure, make available overnight credit in TARGET2 to certain central counterparties that are not licensed as credit institutions.

For this purpose, they must meet the following conditions: 1) provide clearing and settlement services and, in addition, be authorised as central counterparties in accordance with the applicable Union or national legislation; 2) be established in the euro area; 3) be subject to supervision and/or oversight by competent authorities; 4) comply with the oversight requirements for the location of infrastructures offering services in euro, as amended from time to time and published on the ECB's website; 5) have accounts in the Payments Module of TARGET2; and 6) have access to intraday credit.

It is clarified that the guarantee funds that a central counterparty has to maintain under the applicable legislation, including those required on oversight grounds, shall be remunerated at the main refinancing operations rate minus 15 basis points, while other guarantee funds shall be remunerated at the deposit rate.

The Guideline came into force on 3 April 2011 and shall apply from 11 April 2011.

Mergers of public limited liability companies: Union legislation

Directive 2011/35/EU of the European Parliament and of the Council of 5 April 2011 (OJ L of 29 April 2011) concerning mergers of public limited liability companies coordinates the safeguards required in mergers for the protection of the interests of members and others.

The Directive incorporates most of the provisions of Council Directive 2001/23/EC of 12 March 2001 on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses, as well as the provisions on reporting and documentation set out in Directive 2009/109/EC of the European Parliament and of the Council of 16 September 2009[22] amending Council Directives 77/91/EEC, 78/855/EEC and 82/891/EEC, and Directive 2005/56/EC as regards reporting and documentation requirements in the case of mergers and divisions. It thus regulates these transactions with a view to ensuring that third parties are sufficiently informed.

The Member States shall, in accordance with this Directive, make provision for rules governing merger by the acquisition of one or more companies by another company[23] and merger by the formation of a new company.[24]

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21 See «Financial Regulation: 2007 Q3», *Economic Bulletin*, October 2007, Banco de España, pp. 151 and 152.

22 See «Financial Regulation: 2009 Q4», *Economic Bulletin*, January 2010, Banco de España, pp. 164 and 165.

23 "Merger by acquisition" shall mean the operation whereby one or more companies are wound up without going into liquidation and transfer to another all their assets and liabilities in exchange for the issue to the shareholders of the company or companies being acquired of shares in the acquiring company and a cash payment, if any, not exceeding 10% of the nominal value of the shares so issued or, where they have no nominal value, of their accounting par value. A Member State's laws may provide that merger by acquisition may also be effected where one or more of the companies being acquired is in liquidation, provided that this option is restricted to companies which have not yet begun to distribute their assets to their shareholders.

24 "merger by the formation of a new company" shall mean the operation whereby several companies are wound up without going into liquidation and transfer to a company that they set up all their assets and liabilities in exchange for the issue to their shareholders of shares in the new company and a cash payment, if any, not exceeding 10% of the nominal value of the shares so issued or, where they have no nominal value, of their accounting par value. A Member State's laws may provide that merger by the formation of a new company may also be effected where one or more of the companies which are ceasing to exist is in liquidation, provided that this option is restricted to companies which have not yet begun to distribute their assets to their shareholders.

In the case of merger by acquisition, the administrative or management bodies of the merging companies shall draw up draft terms of merger in writing, the content of which is set out in detail in the Directive. Draft terms of merger must be published for each of the merging companies, at least one month before their approval, or made available on its website free of charge for the public or via the central electronic platform referred to in Directive 2009/101/EC.

One or more experts, acting on behalf of each of the merging companies but independent of them, appointed or approved by a judicial or administrative authority, shall examine the draft terms of merger and draw up a written report to the shareholders. However, the laws of a Member State may provide for the appointment of one or more independent experts for all the merging companies, if such appointment is made by a judicial or administrative authority at the joint request of those companies.

In addition to the draft terms of merger, shareholders shall be entitled to receive certain documentation, specified in the Directive, at least one month before the date fixed for the general meeting approving the merger. This documentation includes the annual accounts and annual reports of the merging companies for the preceding three financial years. A company shall be exempt from this requirement if it make such documentation available to the public on its website during that period of time.

A merger shall require at least the approval of the general meeting with a majority of not less than two thirds of the votes attached to the shares, equity units or subscribed capital represented. The laws of a Member State may, however, provide that a simple majority of the votes shall be sufficient when at least half of the subscribed capital is represented.

Protection of the rights of the employees of each of the merging companies shall be regulated in accordance with Directive 2001/23/EC.

The laws of the Member States must provide for an adequate system of protection of the interests of creditors of the merging companies whose claims antedate the publication of the draft terms of merger and have not fallen due at the time of such publication. To that end, such creditors shall be entitled to obtain adequate safeguards where the financial situation of the merging companies makes such protection necessary.

In any event, Member States shall ensure that the creditors are authorised to apply to the appropriate administrative or judicial authority for adequate safeguards provided that they can credibly demonstrate that due to the merger the satisfaction of their claims is at stake and that no adequate safeguards have been obtained from the company.

The Directive sets out the legal consequences of a merger and the civil liability of the administrative or management bodies of the acquiring or acquired company, and limits the cases of nullity of a merger in order to preserve legal certainty in dealings between interested companies, between interested companies and third parties and between shareholders.

Also set forth is the regime governing merger by formation of a new company, which includes most of the provisions laid down for the other type of merger.

Finally, where a merger by acquisition is carried out by a company which holds 90% or more, but not all, of the shares and other securities conferring the right to vote at general

meetings of the company or companies being acquired, Member States shall not require approval of the merger by the general meeting of the acquiring company if certain conditions are fulfilled.

The Directive came into force on 1 July 2011.

Amendment of legislation on the procurement of euro banknotes

Guideline ECB/2011/3 of 18 March 2011 (OJ L of 1 April 2011), amending Guideline ECB/2004/18 of 16 September 2004,[25] on the procurement of euro banknotes was issued in compliance with the requirement to review Guideline ECB/2004/18 at the beginning of 2008 and every 2 years thereafter.

The ECB Governing Council decided on 10 July 2003 that a single Eurosystem tender procedure should apply to the procurement of euro banknotes at the latest from 1 January 2012 onwards. Thus national central banks (NCBs) that have an inhouse printing works, or those using a public printing works may elect not to participate in the single Eurosystem tender procedure. In such cases, these printing works will remain responsible for the production of the euro banknotes that have been allocated to their NCBs in accordance with the capital key but will be excluded from participating in the single Eurosystem tender procedure.

The expected start date of the procedure described above may be changed by a Governing Council decision where more than half of the national central banks (NCBs) representing more than half of the Eurosystem's total banknote printing requirement choose not to participate.

Given that this situation has occurred, Guideline ECB/2011/3 changes the start date of the single Eurosystem tender procedure from 1 January 2012 to 1 January 2014, unless the Governing Council decides on a different start date.

The Guideline came into force on 20 March 2011.

Credit rating agencies: amendment of Union regulation and application to Spanish law

AMENDMENT OF UNION LEGISLATION

Regulation 513/2011 of the European Parliament and of the Council of 11 May 2011 (OJ L of 31 May 2011) amends Regulation 1060/2009 of the European Parliament and of the Council of 16 September 2009[26] on credit rating agencies.

The main change introduced by the Regulation is that it entrusts to the new European Securities and Markets Authority (ESMA)[27] most of the functions relating to the registration, deregistration and ongoing supervision of credit rating agencies, jointly with those of the competent authority of the credit rating agency's home Member State. Previously these powers were shared by the Committee of European Securities Regulators and, where appropriate, the competent authority of that Member State. In general, a noteworthy change from the previous legislation is the reduction of the time period for the ESMA to examine the application for registration submitted by a credit rating agency.

The ESMA is empowered to require credit rating agencies, persons involved in credit rating activities, rated entities and related third parties, third parties to whom the credit rating agencies have outsourced operational functions or activities and persons otherwise closely and

25 See «Financial Regulation: 2004 Q4», *Economic Bulletin*, January 2005, Banco de España, pp. 8 and 9.
26 See «Financial Regulation: 2009 Q4», *Economic Bulletin*, January 2010, Banco de España, pp. 165 and 166.
27 The ESMA was created by Regulation 1095/2010 of the European Parliament and of the Council of 24 November 2010.

substantially related or connected to credit rating agencies or credit rating activities to provide all information that is necessary in order to carry out its duties.

The ESMA may delegate specific supervisory tasks to the competent authority of a Member State, for instance where a supervisory task requires knowledge and experience with respect to local conditions, which are more easily available at national level. The kind of tasks that it has to delegate include the carrying out of specific investigatory tasks and on-site inspections.

The ESMA may impose fines on credit rating agencies, where it finds that there are serious indications of the possible existence of facts liable to constitute one or more of the infringements listed in the Regulation. Fines are imposed according to the level of seriousness of the infringements. For this purpose, the Regulation establishes coefficients linked to aggravating and mitigating circumstances in order to give the ESMA the necessary tools to decide on a fine which is proportionate to the seriousness of an infringement. The ESMA is empowered to take a range of measures, including, but not limited to, requiring the credit rating agency to bring the infringement to an end, suspending the use of credit ratings for regulatory purposes, temporarily prohibiting the credit rating agency from issuing credit ratings and, as a last resort, withdrawing the registration when the credit rating agency has seriously or repeatedly infringed the Regulation.

The ESMA, along with the competent authorities and the sectoral competent authorities, shall cooperate with each other and exchange the information required for the purposes of carrying out their duties. Also, powers are granted to the ESMA (previously to the competent authorities of the Member States) to transmit to the national central banks, the European System of Central Banks and the European Central Bank, in their capacity as monetary authorities, to the European Systemic Risk Board and, where appropriate, to other public authorities responsible for overseeing payment and settlement systems, confidential information intended for the performance of their tasks.

Lastly, exclusive powers are granted to the ESMA (previously to the competent authorities of the Member States) to conclude cooperation agreements on information exchange with the supervisory authorities of third countries, provided that the information disclosed is subject to guarantees of professional secrecy.

The Regulation came into force on 1 June 2011.

APPLICATION OF UNION LEGISLATION

Law 15/2011 of 16 June 2011 (BOE of 17 June 2011) amending certain financial legislation[28] applies to the Spanish legal system Regulation 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies.

The main purpose of the Law is to establish the obligation for certain financial institutions[29] to use the ratings issued by credit rating agencies. Also, the legislation on credit rating agencies is adjusted as necessary for the respective national supervisors to cooperate with the ESMA.

28 Specifically, Law 13/1985 of 25 May 1985 on investment ratios, own funds and reporting requirements for financial intermediaries; Law 24/1988 of 28 July 1988 on the securities market; Law 19/1992 of 7 July 1992 on the legal regime for real estate investment companies, real estate funds and mortgage securitisation special purpose entities, and Law 35/2003 of 4 November 2003 on collective investment institutions.

29 Specifically, the entities concerned are credit insitutitons, investment firms, mortgage securitisation special purpose entities and collective investment institution custodians.

The main amendments made by the Law are as follows:

From the standpoint of solvency, the use by credit institutions or investment firms of external credit ratings shall require that these have been issued or endorsed by an ESMA established in the European Union and registered according to Regulation 1060/2009. Ratings of institutions established or financial instruments issued outside the European Union must have been issued by a credit rating entity established in a non-Member State that has received an equivalent certification in accordance with Regulation 1060/2009.

The credit rating agency must have been recognised by the Banco de España or, where applicable, by the CNMV, in accordance with the criteria established for this purpose and, in turn, considering the objectivity, independence, transparency and ongoing review of the methodology applied, as well as the market credibility and acceptance of the credit ratings issued by that credit rating agency.

The CNMV supervision, inspection and sanctioning regime established in Securities Market Law 24/1988 of 28 July 1988 shall apply to: 1) the credit rating agencies established in Spain and registered in accordance with Regulation 1060/2009, persons involved in credit rating activities, rated entities and related third parties, third parties to whom the credit rating agencies have outsourced certain functions or activities, and other persons otherwise related or connected to credit rating agencies or credit rating activities, and 2) the credit rating agencies registered by a competent authority of the European Union, and the credit rating agencies registered by a competent authority of a third country that have received certification based on equivalence under said Regulation, and which in both cases operate in Spain.

The CNMV shall exercise its authority and apply the infringement and sanctioning regime pursuant to Law 24/1988 in accordance with European Union legislation on credit rating agencies. It shall have the necessary supervision and inspection powers to perform the functions assigned by delegation or under cooperation arrangements with other competent authorities, in accordance with the provisions of Regulation 1060/2009.

The CNMV shall cooperate with and assist other competent authorities of the European Union to carry out the functions set out in Regulation 1060/2009. In particular it may request the cooperation of other competent authorities of the European Union in a supervisory activity, for an on-the-sport verification or an investigation of, inter alia, matters relating to credit rating agencies.

Lastly, the CNMV shall maintain, in addition to the official registers set out in Law 24/1988, which shall be freely available to the public, a register of credit rating agencies established in Spain.

The Law came into force on 18 June 2011.

Amendment of rules on reporting by foreign collective investment institutions registered with the CNMV

CNMV Circular 2/2011 of 9 July 2011 (BOE of 26 July 2011) on reporting by foreign collective investment institutions registered with the CNMV repeals and replaces CNMV Circular 2/2006 of 27 June 2006.[30] The Circular writes into the Spanish legal system the latest

30 See «Financial Regulation: 2006 Q3», *Economic Bulletin*, October 2006, Banco de España, pp. 7 and 8.

precepts of Union legislation[31] which came into force on 1 July 2011.

Under the new notification procedure, collective investment institutions (CIIs) have to submit the relevant documentation to the competent authority of the home Member State. That documentation shall include the notification letter, which contains the identity of the entity empowered to represent the CII before the CNMV and the information on the provisions for marketing the CII in the host Member State. In this respect, the Circular spells out the specific information which the foreign CII must include in the notification letter, for which purpose it sets out a standard format of the marketing report.[32]

Certain information on the foreign CII must be kept up to date electronically.

The requirements regarding the CII documentation to be sent to the CNMV are changed, the information required to be disclosed to investors is adjusted somewhat, the requirement to register compartments in the CNMV register is eliminated, and the content of the communication to be made to the CNMV pursuant to Article 52 of the Personal Income Tax Regulations is broadened to include information on compartments and/or classes to be reported for tax purposes.

Lastly, non-harmonised CIIs are no longer required to send information electronically.

The Circular came into force on 1 July 2011.

Categories of collective investment institutions based on investment policy: amendment of legal provisions

CNMV Circular 3/2011 of 9 June 2011 (BOE of 27 June 2011) amended CNMV Circular 1/2009 of 4 February 2009[33] on CII categories based on investment policy.

The CII types established for the purpose of defining CII categories are changed as regards listed funds, being reclassified as listed CIIs so as to include the listed index SICAV (open-end investment company) created by Royal Decree 749/2010 of 7 June 2010 amending the implementing regulations of Law 35/2003 of 4 November 2003 on CIIs approved by Royal Decree 1309/2005 of 4 November 2005.

The calculation of the investment percentages which define the various investment policies is changed. Previously the net assets of the CII were taken as the base for the calculation, whereas now the total exposure of the CII is used.

For this purpose, the total exposure is defined as the sum of the exposure obtained by the CII through its investments in spot and derivative financial instruments. To calculate the

31 Specifically, Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS), which, among other things, established a new notification procedure for harmonised foreign collective investment institutions, in order to facilitate access by them to the markets of other Member States, and Commission Regulation 584/2010 of 1 July 2010 implementing Directive 2009/65/EC of the European Parliament and of the Council as regards the form and content of the standard notification letter and UCITS attestation, the use of electronic communication between competent authorities for the purpose of notification, and procedures for on-the-spot verifications and investigations and the exchange of information between competent authorities, and Commission Directive 2010/42/EU of 1 July 2010 implementing Directive 2009/65/EC of the European Parliament and of the Council as regards certain provisions concerning fund mergers, master-feeder structures and notification procedure.

32 The letter must include the following information: a) identity of the foreign CII; b) name of the compartments or subfunds marketed in Spain with more than 500 shareholders and of the share classes forming part of those compartments or subfunds; c) ISIN code numbers of the CII, compartments or subfunds and, where applicable, share classes; d) total number of shareholders of the compartment or subfund; e) total assets of the foreign CII or of the compartment or subfund; and f) date of reference of the information communicated.

33 See «Financial Regulation: 2009 Q1», *Economic Bulletin*, April 2009, Banco de España, pp. 194 and 195.

exposure through derivatives, use shall be made of the commitment methodology set out in CNMV Circular 6/2010 on transactions in derivatives of CIIs. Furthermore, investments in equity securities issued by non-euro area entities and currency risk shall also be considered in terms of total exposure.

Lastly, solely for the purpose of determining investment policy, no additional exposure for the CII is considered to arise if its investments in spot or derivative financial instruments do not expose it to additional risk, including but not limited to, interest rate risk and credit risk. Hence they must be in, for example, public debt issued by a State of high credit quality or repos on these assets, the maturities of which are below three months.

The Circular came into force on 27 August 2011.

New legislation on consumer credit agreements

Law 16/2011 of 24 June 2011 (BOE of 25 June 2011) on credit agreements for consumers wrote into Spanish law Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealed Law 7/1995 of 23 March 1995 on consumer credit.

Like the previous law, this Law applies to those contracts whereby a creditor grants or promises to grant to a consumer credit in the form of a deferred payment, loan, credit line or other similar financial accommodation. The term "consumer" means a natural person who is acting for purposes which are outside his trade, business or profession.

The following contracts, inter alia, are excluded from the scope of this Law: a) credit agreements which are secured by a real estate mortgage; b) credit agreements the purpose of which is to acquire or retain property rights in land or in an existing or projected building; c) credit agreements involving a total amount of credit less than €200 (previously €150); d) hiring or leasing agreements where an obligation to purchase the object of the agreement is not laid down either by the agreement itself or by any separate agreement; e) credit agreements in the form of an overdraft facility and where the credit has to be repaid within one month; f) credit agreements where the credit is granted free of interest and without any other charges and credit agreements under the terms of which the credit has to be repaid within three months and only insignificant charges are payable (1% of the total credit amount); and g) credit agreements where the credit is granted by an employer to his employees as a secondary activity free of interest or at annual percentage rates of charge lower than those prevailing on the market.[34] However, the partial application of the Law to credit agreements of total amount exceeding €75,000 (previously €18,030) remains in place.

In order to improve consumer information, the Law addresses what takes place before the consumer concludes a credit agreement. Specifically, it regulates in detail the basic information to be included in advertising, in business communications and in the announcements of offers displayed in commercial premises proposing either a credit or the services of an intermediary to conclude a credit agreement.

Also set forth is a list of the credit features about which the creditor and, if applicable, the credit intermediary must inform the consumer before he is bound by any credit agreement or offer. Such information shall be provided by means of the Standard European Consumer Credit Information form set out in the annexes to this Law.

34 Annual percentage rates of charge lower than those prevailing on the market are defined as those below the legal interest rate.

Creditors and, if applicable, intermediaries must help the consumer to decide which credit agreement, within the range of products proposed, is the most appropriate for his needs and financial situation. This assistance specifically entails an obligation to explain to the consumer in a personalised manner the characteristics of the products proposed and the related pre-contractual information and to warn him of the risks attaching to default on payment and to over-indebtedness. so that he can understand the effects which they may have on his economic situation.

If the obtainment of credit on the terms and conditions offered is linked by the creditor to the conclusion of a contract for ancillary services, in particular insurance, the creditor must inform the consumer of this circumstance and of its cost, and also of the terms and conditions which would otherwise be applied to the credit agreement should the contract for ancillary services, in particular insurance, not be concluded.

The creditor must assess the consumer's creditworthiness prior to the conclusion of the credit agreement, for which purpose it may use information obtained from its own sources and that furnished by the consumer, including the consultation of certain databases.[35] Although this assessment is compulsory, its scope is left to the discretion of the creditor depending on the commercial relationship between it and its customer. The assessment of consumer creditworthiness by credit institutions shall also take account of specific risk management and internal control rules applicable to them under the related specific legislation.

Where a decision to reject an application for credit is based on the consultation of a relevant database, the creditor must, immediately and at no cost, inform the consumer of the results of the consultation and of the details of the database. Database managers must provide creditors from other Member States with access to their databases for assessing the creditworthiness of consumers. The conditions for access shall be non-discriminatory for Spanish creditors.

The increased interest of consumers in knowing their rights and obligations is reflected in the regulation of the content of credit agreements, which takes into account the specific features of the various kinds of credit agreement.

In the contract termination phase, the Law regulates the right of the contracting parties to terminate an open-end credit agreement, the consumer's right to repay the credit early and the borrower's position in the event of assignment of the creditor's rights under a credit agreement, which had been established in Law 7/1995 and now has its precedent in the transposed Directive. It also introduces the consumer's right of withdrawal from a credit agreement, the regulation of which follows the criteria governing the exercise of this right in the distance marketing of financial services.

The mathematical formula for calculating the annual percentage rate is intended to define clearly and comprehensively the total cost of a credit to the consumer,[36] and to ensure that its definition is comparable in all Member States of the European Union. The formula is set

35 The credit and creditworthiness records referred to in Organic Law 15/1999 of 13 December 1999 on the Protection of Personal Data, subject to the conditions, requirements and assurances envisaged in said Organic Law and its implementing regulations.

36 Excluded are any charges payable by the consumer for non-compliance with any of his commitments laid down in the credit agreement and charges other than the purchase price which, for purchases of goods or services, he is obliged to pay whether the transaction is effected in cash or on credit.

out in the annexes to the Law, as are the assumptions for its calculation. However, in accordance with Directive 2008/48/EC the Ministry of Economic Affairs and Finance is empowered to establish additional assumptions or change existing ones if the assumptions included in the Law do not suffice to calculate said rate in a uniform manner or are not adapted any more to the commercial situation at the market.

Certain provisions of Law 7/1995 enhancing protection in the area of consumer credit are retained although they are not required by Union legislation, such as those relating to binding offers, the effectiveness of contracts linked to the obtainment of credit, improper charging and penalties for non-compliance with formalities and for omission of compulsory clauses in contracts.

As regards the penalty regime, non-compliance by credit institutions with the requirements of this Law are penalised under the law on discipline and supervisory intervention of credit institutions.[37] Non-compliance by other natural and legal persons is an infringement of consumer and user protection requirements.[38]

The regime governing appeals provides for an out-of-court complaint and redress mechanism to resolve disputes between consumers and creditors or credit intermediaries, and incorporates the regulation of injunctions against unlawful conduct.

The Law came into force on 25 September 2011.

8.7.2011.

37 Law 26/1988 of 29 July 1988 on the discipline and intervention of credit institutions.

38 The General Consumer and User Protection Law and other supplementary laws, enacted by Legislative Royal Decree 1/2007 of 16 November 2007, and other applicable legislation, as well as regional government legislation.